

Finolex Industries Ltd.

No. of shares (m)	124.1
Mkt cap (Rs crs/\$m)	4968/655.5
Current price (Rs/\$)	400/5.3
Price target (Rs/\$)	480/6.3
52 W H/L (Rs.)	635/283
Book Value (Rs/\$)	184/2.4
Beta	0.8
Daily volume NSE (avg. monthly)	36590
P/BV (FY20e/21e)	2.4/2.2
EV/EBITDA (FY20e/21e)	8.6/12.1
P/E (FY20e/21e)	13.1/20.2
EPS growth (FY19/20e/21e)	23.2/0.5/-33.6
OPM (FY19/20e/21e)	19.5/15.9/15.5
ROE (FY19/20e/21e)	14.7/16.9/11.7
ROCE (FY19/20e/21e)	14.5/15.3/11.7
D/E ratio (FY19/20e/21e)	0.0/0.0/0.0
BSE Code	500940
NSE Code	FINPIPE
Bloomberg	FNXP IN
Reuters	FINX.NS

Shareholding pattern

	%
Promoters	52.5
MFs / Banks / FIs/Others	12.7
FPIs	2.3
Govt. Holding	0.0
Public & Others	32.5
Total	100.0

As on Mar 31, 2020

Recommendation

BUY

Analyst

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Company Brief

Headquartered in Pune, Finolex Industries is one of India's leading manufacturers of pvc -U pipes & fittings and pvc resin. Its pipes and fittings is largely used in the agriculture segment.

Highlights

- Robust growth of Finolex's non-agri pipes business did little to circumvent patchy of take of its agri pipes (impacted by longer monsoons) for overall PVC pipes & fittings volumes plunged by a distressing 10.8% to 52815 tons compared to 59179 tons in the same quarter a year ago, erasing much of the gains observed in Q1 when volumes surge by a barely subdued 18.1%. For all the babble regarding humungous market opportunities in CPVC market, Finolex's CPVC volumes make up less than 5% of overall volumes - CPVC grew by 9.1% in Q3.
- Trampled by over 10% fall in both external sales of PVC resins and PVC pipes & fittings, PBT advanced by a measly 3.1% to Rs 124.63 crs compared to Rs 120.93 crs but lower tax provisions fostered 18.5% growth in post tax earnings. PVC/EDC delta barely remained elevated at \$589, though higher than \$535 in the same period last fiscal and \$ 583 in Q2. Consequently, Finolex's PVC business EBIT rose by a puny 1.1% Rs 81.82 crs in Q3.
- No meager fall in global crude oil prices has visibly depressed PVC prices in last few months, suppressing PVC/EDC delta further in Q1 of current fiscal from ~\$560 in Q4. Risks looms on dramatic cutback in planned capex of Rs 100-150 crs for FY21 not least due to excruciating demand stress in Q1 of current fiscal, all thanks to national lockdowns. Challenges in managing logistics and labor shortage have anything but helped meet pipe demand from agriculture sector. Partial commencement of PVC pipes & fittings would barely help alleviate prevailing demand stress for pipes.
- The stock currently trades at 13.4x FY20e EPS of Rs 29.80 and 20.2x FY21e EPS of Rs 19.80. Hamstrung by motley of factors including economic stress due to Covid 19 and gut-wrenching fall in crude oil prices, post tax earnings would tumble by a third this fiscal on dismal return on capital. Yet sustainable competitive positioning such as backward integration in PVC pipes and remarkable distribution network would foster faster rebound in earnings. Further GOI's forceful impetus on building water infrastructure and urban and rural housing would barely stymie demand for PVC pipes. On balance, we maintain our buy recommendation on the stock with revised target of Rs 480 (previous target: Rs 662) based on 24x FY21e earnings.

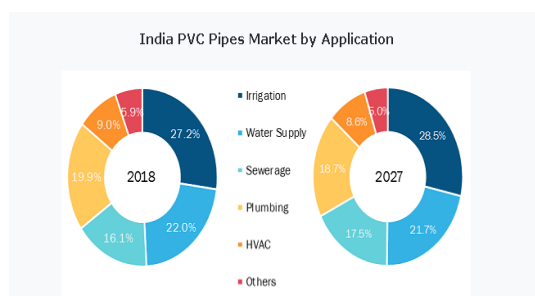
(Figures in Rs crs)	FY17	FY18	FY19	FY20e	FY21e
Income from operations	2602.36	2737.79	3091.32	3100.92	2195.40
Other Income	24.32	25.32	41.57	36.13	48.19
EBITDA (other income included)	587.39	509.25	617.97	530.66	388.54
Profit after EO	352.18	298.82	368.05	369.84	245.71
EPS (Rs)	28.38	24.08	29.66	29.80	19.80
EPS growth (%)	51.6	-15.2	23.2	0.5	-33.6

Investment Thesis

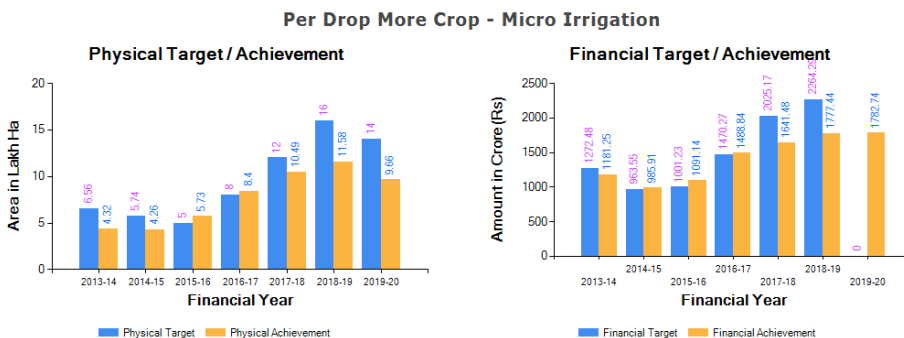
PVC Industry

According to a report by ResearchAndMarkets.com, the Indian PVC pipes market is estimated to grow at a CAGR of 4.5% during 2018-27 to reach \$5209 mn by the terminal year. Rising demand for PVC pipes from agriculture, automotive, building and construction, electrical and other end use industries is expected to propel the growth of Indian PVC pipes market during the forecasted period. Rise in level of implementation of growth oriented government schemes in end-user application sectors will majorly contribute to this growth. Surge in housing demand fostered by rising population and increasing disposable incomes will drive the growth in Indian ground handling services market.

ResearchAndMarkets.com also contends the PVC pipes market in India is still at a early growth stage with a large number of organized and unorganized players competing for market share. The market, which grew by double digit during 2013-18, has benefitted from rising Government of India's investments in irrigation, housing and sanitation through scheme such as Housing for All, AMRUT and PMKSY. Of the major end-user applications like irrigation, sewage, water-supply, plumbing and bore well, irrigation has the largest revenue share not least due to widespread use of PVC pipes and fittings in irrigation systems installed in farms and fields across the country.



Source: ResearchAndMarkets.com



Source: PMKSY

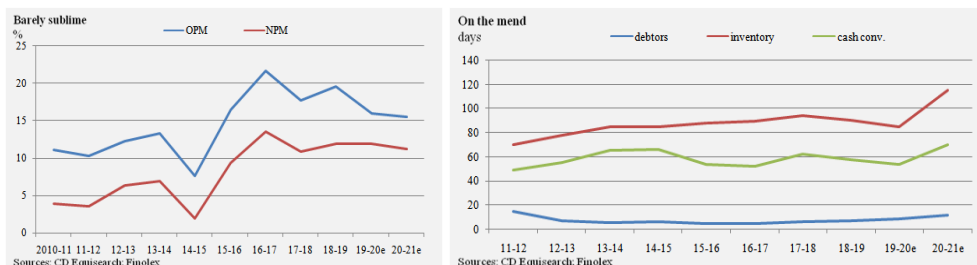
The Indian agriculture sector is poised for good times ahead not least due to increased government investments in agricultural facilities such as irrigation systems, warehousing, and cold storage. Further, rising domestic income coupled with increasing demand for food would propel the Indian PVC pipes market growth. Also the PVC pipe is quite economical and versatile as these can be used in numerous structures which support its market growth.

Financials & Valuation

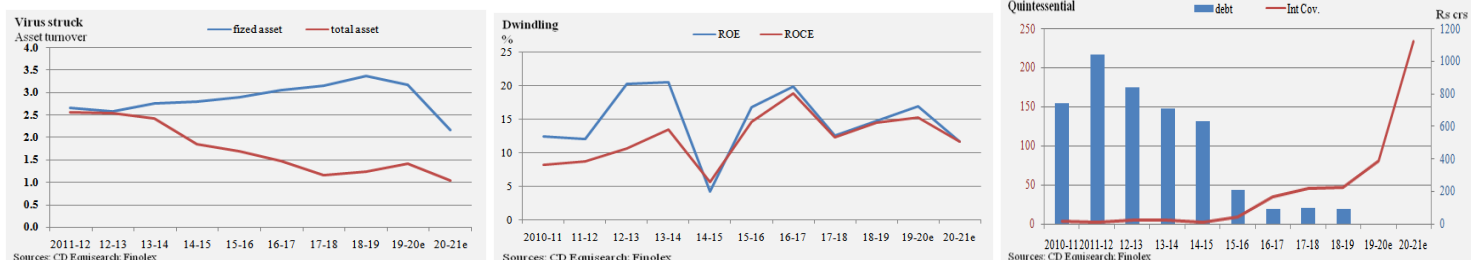
Recommencement of Finolex's plants at Ratnagiri, Urse and Masar would do little to discernibly foster production for demand continues to remain subdued even after relaxations in lockdown. Fearing stress in volumes, Finolex plans to cut capex this fiscal from the earlier planned Rs 100-150 crs. Poor of take of PVC pipes & fittings in Q1 - accounts for over 30% of annual volumes - would escalate volume decline to 23% in the current fiscal - sharpest decline in more than a decade. External sales of PVC resins would drop by some 11% this fiscal after a projected decline of over 12% in FY20 - was down by 12.5% in 9MFY20, thus catapulting capacity utilization of Finolex's resin capacity to 74% in FY21 from some 95% in FY19.

CD Equiresearch Pvt Ltd

Though demand for agri -pipes has not been very subdued so far this fiscal but logistical challenges and labour shortage have restrained volume off take. Fall in crude oil prices, of late, would betray itself in lower PVC resin prices with resultant drop in prices of PVC pipes. Revenues as a consequence of both lower volumes and depressed realizations are projected to decline by nearly 30% this fiscal. Yet recovery would scarcely stagger not least due to Government of India's ambitious investments in irrigation, housing and sanitation through scheme such as Housing for All, AMRUT and PMKSY.

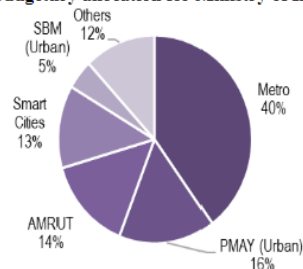


Despite softening EDC prices, Finolex's PVC/EDC spread would barely sustain over \$550 in current fiscal. Post tax earnings would decline by over 33% but on stable margins. Tepid utilization coupled with depressed polymer prices would pummel Finolex's fixed asset turnover to lowest level in a decade. ROE would abysmally drop to 11.7% from 16.9% in FY20 and four average of some 16%. Yet measurable gains in working capital are expected this fiscal.

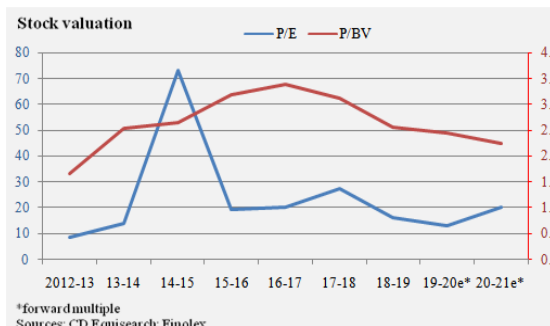


The stock currently trades at 13.4x FY20e EPS of Rs 29.80 and 20.2x FY21e EPS of Rs 19.80. Near term stress in earnings accentuated by national lockdowns and appalling drop in crude oil prices, could do little to obscure Finolex's envious competitive advantage in PVC resin manufacturing and GOI's ambitious programs to promote housing, irrigation and water infrastructure. Though PVC pipes & fittings volumes, particularly, non-agri, would not gainfully recover in next few months, its vast distribution network coupled with its deleveraged balance sheet would doubtlessly lend immense resilience. Due to prevailing economic stress, current year EPS estimates have been slashed by nearly 40%. Weighing odds, we maintain our buy recommendation on the stock with revised target of Rs 480 (previous target: Rs 662) based on 24x FY21e earnings. More info refer to our December report.

Budgetary allocation for Ministry of Housing and Urban Affairs (2020-21)



Sources: Notes on Demand for Grants 2020-21, Ministry of Housing and Urban Affairs; PRS.



Cross Sectional Analysis

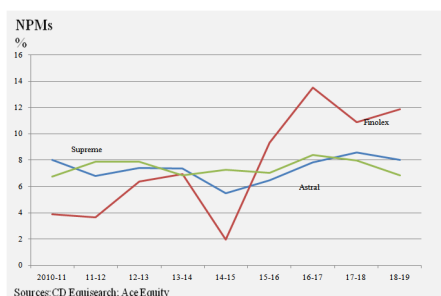
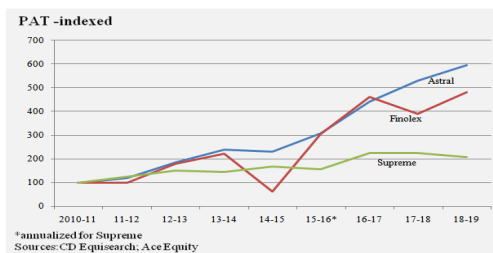
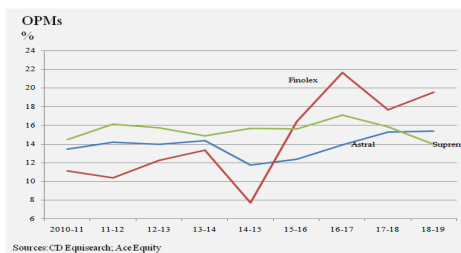
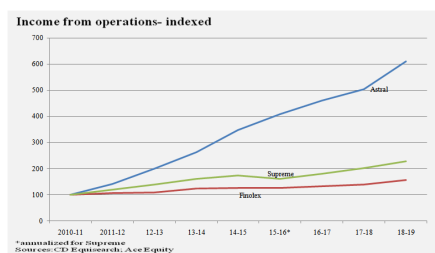
Company	Equity*	CMP	Mcap*	Sales*	Profit*	OPM (%)	NPM (%)	Int. Cov.	ROE (%)	DER	Mcap / sales	P/BV	P/E
Astral Poly	15	840	12656	2578	250	17.2	9.7	8.8	22.0	0.1	4.9	10.1	50.7
Finolex Ind.	124	400	4968	3184	360	15.4	11.3	87.9	14.6	0.00	1.6	2.2	13.8
Supreme Inds	25	979	12431	5512	467	15.1	7.9	31.2	21.9	0.2	2.3	5.5	26.6

*figures in crores; calculations on ttm basis

Book value adjusted for goodwill and revaluation reserves where applicable

National lockdown distressingly impacted pipe volumes of Astral for it reported a 58% drop in its dispatches in March (compared to the same month a year ago) taking the overall decline to 17% for the quarter. Volumes, however, for the full year rose by 7.5% to 1.32 lakh mt. Overall capacity utilization tumbled from 59.9% to 55.4% in FY19 as production advanced by a barely modest 12.3% on yoy basis. Despite stress in revenues in Q4 (consolidated revenues down by 18.8%) operating profit slid just 5.4% not least due to no smallish gains in raw material costs. PBT, however, declined by 30.5% to Rs 65.7 crs and PAT by 17.4% compared to that a year ago. Its plastic business better than its adhesives for it reported 5% drop in EBIT in Q4 compared to 35.4% for adhesives.

Dramatic savings in raw material costs helped Supreme Industries post 35.4% growth in operating profit (despite 6.6% fall in revenues), thus helping 43.8% surge in PBT (before associate profit) in Q4. Remarkable gain in profitability was reported by its plastic piping products business for it reported 77.7% growth in EBIT on flat sales. Yet overall plastic goods sold declined by 9.5% to 1.03 lakh tons compared to 1.14 lakh tons in the same quarter a year ago. Its flagship plastic piping business posted a modest 7.5% growth in its volumes to 3.01 lakh tons last fiscal, while its industrial products business witnessed a decline of 13.3%, taking the overall volume growth to a meager 3.4%. Both plastic piping and consumer products businesses reported smart gains in margins last fiscal.



Financials

Quarterly Results

	Figures in Rs crs					
	Q3FY20	Q3FY19	% chg.	9MFY20	9MFY19	% chg.
Income from operations	699.40	756.61	-7.6	2219.87	2127.08	4.4
Other Income	6.73	3.32	102.7	29.86	29.32	1.8
Total Income	706.13	759.93	-7.1	2249.73	2156.40	4.3
Total Expenditure	560.97	617.67	-9.2	1875.87	1697.17	10.5
EBIDTA (other income incl.)	145.16	142.26	2.0	373.86	459.23	-18.6
Interest	1.77	1.71	3.6	2.88	9.92	-71.0
Depreciation	18.76	19.63	-4.4	54.93	52.40	4.8
PBT	124.63	120.93	3.1	316.05	396.90	-20.4
Tax	31.31	42.20	-25.8	47.56	138.49	-65.7
Net Profit	93.32	78.73	18.5	268.49	258.42	3.9
Extraordinary Item	-	-	-	0.00	-18.21	-100.0
Adjusted Net Profit	93.32	78.73	18.5	268.49	276.63	-2.9
EPS	7.52	6.34	18.5	21.64	22.29	-2.9

Segment results

	Figures in Rs crs					
	Q3FY20	Q3FY19	% chg.	9MFY20	9MFY19	% chg.
Segment Revenue						
PVC	408.03	484.03	-15.7	1245.57	1314.78	-5.3
PVC Pipes & Fittings	553.51	590.62	-6.3	1921.76	1783.68	7.7
Total	961.54	1074.65	-10.5	3167.33	3098.46	2.2
Less: Inter-segment revenue	262.14	318.04	-17.6	947.46	971.38	-2.5
Income from operations	699.40	756.61	-7.6	2219.87	2127.08	4.4
Segment EBIT						
PVC	81.82	80.88	1.2	168.26	296.23	-43.2
PVC Pipes & Fittings	43.56	43.80	-0.5	139.76	121.66	14.9
Total	125.38	124.68	0.6	308.02	417.89	-26.3
Interest	1.77	1.71	3.6	2.88	9.92	-71.0
Unallocable exp.(net of income)	-1.02	2.05	-149.6	-10.91	11.07	-198.5
PBT	124.63	120.93	3.1	316.05	396.90	-20.4

Income Statement

Figures in Rs crs

	FY17	FY18	FY19	FY20e	FY21e
Income from operations	2602.36	2737.79	3091.32	3100.92	2195.40
<i>Growth (%)</i>	4.9	5.2	12.9	0.3	-29.2
Other Income	24.32	25.32	41.57	36.13	48.19
Total Income	2626.69	2763.11	3132.89	3137.04	2243.59
Total Expenditure	2039.30	2253.86	2514.93	2606.38	1855.05
EBIDTA (other income incl.)	587.39	509.25	617.97	530.66	388.54
Interest	15.38	9.82	12.27	5.72	1.41
EBDT	572.01	499.44	605.69	524.95	387.13
Depreciation	55.05	60.60	70.08	73.46	58.77
Tax	164.78	140.29	185.82	81.65	82.65
Net Profit	352.18	298.54	349.80	369.84	245.71
EO	0.00	-0.27	-18.25	-	-
Adjusted Net Profit	352.18	298.82	368.05	369.84	245.71
EPS (Rs)	28.38	24.08	29.66	29.80	19.80

Segment results

Figures in Rs crs

	FY17	FY18	FY19	FY20e	FY21e
Segment Revenue					
PVC	770.76	502.57	516.52	448.11	343.82
PVC Pipes & Fittings	2216.87	2328.84	2574.80	2652.81	1851.58
Power	0.00	0.00	0.00	0.00	0.00
Total sales	2987.64	2831.41	3091.32	3100.92	2195.40
Segment EBIT					
PVC	354.68	348.76	377.28	252.26	164.90
PVC Pipes & Fittings	177.41	136.17	182.82	194.59	134.24
Power	32.90	0.00	0.00	0.00	0.00
Total	564.99	484.92	560.09	446.85	299.14
Interest	15.38	9.82	12.27	5.72	1.41
Unallocable exp.(net of income)	32.64	36.28	12.20	-10.36	-30.63
PBT	516.96	438.83	535.62	451.49	328.36

Balance Sheet

Figures in Rs crs

	FY17	FY18	FY19	FY20e	FY21e
SOURCES OF FUNDS					
Share Capital	124.10	124.10	124.10	124.10	124.10
Reserves	2167.30	2640.47	2404.33	1865.96	2215.17
Total Shareholders Funds	2291.39	2764.57	2528.42	1990.05	2339.27
Long term debt	0.00	0.00	0.00	0.00	0.00
Total Liabilities	2291.39	2764.57	2528.42	1990.05	2339.27
APPLICATION OF FUNDS					
Gross Block	1982.35	2063.71	2199.44	2,329.44	2,399.44
Less: Accumulated Depreciation	1127.22	1179.47	1248.55	1,322.01	1,380.78
Net Block	855.13	884.24	950.89	1007.43	1018.66
Capital Work in Progress	21.75	90.34	90.25	40.00	30.00
Investments	1222.17	1555.24	1303.03	717.79	1121.31
Current Assets, Loans & Advances					
Inventory	557.40	611.55	620.47	600.00	570.00
Sundry Debtors	52.49	43.14	74.31	70.00	72.00
Cash and Bank	16.34	23.43	29.10	23.89	27.98
Loans and Advances	46.48	76.33	103.48	62.15	52.18
Total CA & LA	672.72	754.45	827.36	756.04	722.17
Current Liabilities	458.22	489.64	513.05	441.29	455.51
Provisions	1.23	1.43	2.40	2.50	2.50
Total Current Liabilities	459.45	491.07	515.45	443.79	458.01
Net Current Assets	213.27	263.38	311.91	312.25	264.15
Net Deferred Tax	-131.61	-120.68	-151.33	-116.51	-126.51
Other Assets (Net Of Liabilities)	110.69	92.06	23.68	29.10	31.65
Total Assets	2291.39	2764.57	2528.42	1990.05	2339.27

Key Financial Ratios

	FY17	FY18	FY19	FY20e	FY21e
Growth Ratios (%)					
Revenue	4.9	5.2	12.9	0.3	-29.2
EBIDTA (other income included)	34.7	-13.2	26.7	-17.8	-26.8
Net Profit	51.6	-15.2	23.2	0.5	-33.6
EPS	51.6	-15.2	23.2	0.5	-33.6
Margins (%)					
Operating Profit Margin	21.6	17.7	19.5	15.9	15.5
Gross Profit Margin	22.0	18.3	20.5	16.9	17.6
Net Profit Margin	13.5	10.9	11.9	11.9	11.2
Return (%)					
ROCE	18.9	12.4	14.5	15.3	11.7
ROE	19.9	12.6	14.7	16.9	11.7
Valuations					
Market Cap / Sales	2.8	3.0	2.0	1.6	2.3
EV/EBIDTA	12.3	16.1	9.1	8.6	12.1
P/E	20.4	27.4	16.5	13.1	20.2
P/BV	3.4	3.1	2.6	2.4	2.2
Other Ratios					
Interest Coverage	34.6	45.7	46.9	80.0	233.4
Debt-Equity Ratio	0.0	0.0	0.0	0.0	0.0
Current Ratio ^a	1.2	1.3	1.6	2.3	2.2
Turnover Ratios					
Fixed Asset Turnover	3.1	3.1	3.4	3.2	2.2
Total Asset Turnover	1.5	1.2	1.2	1.4	1.0
Debtors Turnover	74.2	57.3	52.6	43.0	30.9
Inventory Turnover	4.1	3.9	4.0	4.3	3.2
Creditors Turnover	8.7	9.4	9.3	9.2	6.5
WC Ratios					
Debtor days	4.9	6.4	6.9	8.5	11.8
Inventory days	89.9	94.7	90.4	85.5	115.1
Creditor days	42.1	38.7	39.2	39.8	56.6
Cash conversion cycle	52.7	62.3	58.1	54.1	70.3

Cumulative Financial Data

	FY13-15	FY16-18	FY19-21e
Income from operations	7074	7822	8388
Operating profit	781	1454	1439
EBIT	702	1367	1363
PBT	514	1297	1343
PAT	355	883	984
Dividends	211	471	423
PVC pipe sales (lakh tons)	5.4	6.7	7.3
PVC resin production (lakh tons)	7.4	7.6	7.1
PVC resin sales (lakh tons)	3.62	2.61	1.77
OPM (%)	11.0	18.6	17.2
NPM (%)	5.0	11.3	11.7
Interest coverage	3.7	19.6	70.2
ROE (%)	12.1	14.9	13.6
ROCE (%)	9.0	13.3	13.0
Fixed asset turnover	2.9	3.0	2.9
Debtors turnover	49.3	56.8	48.6
Inventory turnover	4.7	3.6	3.9
Creditors turnover	12.7	9.4	8.6
Debtors days	7.4	6.4	7.5
Inventory days	77.0	100.6	93.1
Creditor days	28.7	38.7	42.6
Cash conversion cycle	55.7	68.3	58.0
Dividend payout ratio (%)	59.5	52.0	43.9

FY13-15 implies three years ending fiscal 15; *as on terminal year

Struck by no smallish effect of virus and dreadful plunge in crude oil prices in last few months, Finolex Industries would doubtlessly struggle to recoup lost PVC pipes & fittings volumes in the first quarter of current fiscal - a no small quarter by any measure for it contributes 30-35% to annual volumes. Cumulative PVC pipes & fittings volumes in FY19-21e period ,as a result, would grow by sub-10% from that in the preceding three year period (see table). Dismal volumes would continue to manifest it in lower margins for OPMs would measurably slide to 17.2% in FY19-21e period compared to 18.6% in the preceding three year period.

Excruciating stress in consumer demand - particularly for non-agri pipes in post Covid period - would do little to galvanize return on capital - ROE estimated at 13.6% for FY19-21e period compared to 14.9% in FY16-19 period - for external sales of PVC resins would remarkably tumble to weak demand (1.77 lakh tons in FY19-21e period Vs 2.61 lakh tons) from user industries. PVC resin realizations have been scarcely buoyant not least due to nerve-wracking fall in global crude oil prices. Vivacious interest coverage ratio betrays relentless efforts to deleverage the balance sheet. Scarcely modest fall in crude oil prices would have a favorable bearing on working capital for cash conversion cycle is estimated to discernibly improve to 58 days from over 68 days (see table).

Financial Summary – US dollar denominated

million \$	FY17	FY18	FY19	FY20e	FY21e
Equity capital	19.1	19.1	17.9	16.5	16.4
Equity shareholders' funds	326.9	402.0	343.9	264.0	292.3
Total debt	14.5	15.5	13.1	0.3	0.7
Net fixed assets (incl CWIP)	135.2	149.8	150.5	138.9	138.4
Investments	188.5	239.1	188.4	95.2	148.0
Net current assets	6.4	17.5	23.5	41.4	18.5
Total assets	326.9	402.0	343.9	264.0	292.3
Revenues	387.9	424.8	442.3	437.5	289.7
EBITDA	87.6	79.1	92.4	74.9	51.3
EBDT	85.3	77.6	90.7	74.1	51.1
PBT	77.1	68.2	80.6	63.7	43.3
PAT	52.5	46.4	52.7	52.2	32.4
EPS(\$)	0.42	0.37	0.42	0.42	0.26
Book value (\$)	2.63	3.24	2.77	2.13	2.36

income statement figures translated at average rates; balance sheet and cash flow at year end rates; projections at current rate (\$75.79/\$)

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buy: >20% accumulate: >10% to ≤20% hold: ≥-10% to ≤10% reduce: ≥-20% to <-10% sell: <-20%

Exchange Rates Used- Indicative

Rs/\$	FY17	FY18	FY19	FY20
Average	67.09	64.45	69.89	70.88
Year end	64.84	65.04	69.17	75.39

All \$ values mentioned in the write-up translated at the average rate of the respective quarter/ year as applicable. Projections converted at current exchange rate. Cumulative dollar figure is the sum of respective yearly dollar value.